



**Mastech Digital Inc.**  
**Q3 2021 Results – Earnings Call**  
**October 27, 2021**

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**Operator**

Greetings, and welcome to Mastech Digital Inc. Q3 2021 Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press “\*” “0” on your telephone keypad. Please note, this conference is being recorded. It is now my pleasure to introduce your host, Jennifer Ford Lacey, Manager of Legal Affairs for Mastech Digital Inc. Thank you, Ms. Ford. Lacey, you may begin.

**Jennifer Ford Lacey**

Thank you, Operator, and welcome to Mastech Digital's third quarter 2021 conference call. If you have not yet received a copy of our earnings announcement, it can be obtained from our website at [www.mastechdigital.com](http://www.mastechdigital.com). With me on the call today are Vivek Gupta, Mastech Digital's Chief Executive Officer; Paul Burton, Mastech InfoTrellis Chief Executive; and Jack Cronin, our Chief Financial Officer.

I would like to remind everyone that statements made during this call that are not historical facts are forward-looking statements. These forward-looking statements include our financial growth and liquidity projections, as well as statements about our plans, strategies, intentions, and beliefs concerning the business, cash flows, costs, and the markets in which we operate.

Without limiting the foregoing, the words believes, anticipates, plans, expects, and similar expressions are intended to identify certain forward-looking statements. These statements are based on information currently available to us and we assume no obligation to update these statements as circumstances change.

There are risks and uncertainties that could cause actual events to differ materially from these forward-looking statements, including those listed in the company's 2020 annual report on Form 10-K filed with the Securities and Exchange Commission and available on its website at [www.sec.gov](http://www.sec.gov).

Additionally, management has elected to provide certain non-GAAP financial measures to supplement our financial results presented on a GAAP basis. Specifically, we will not — we will provide non-GAAP net income and non-GAAP diluted earnings per share data, which we believe

will provide greater transparency with respect to the key metrics used by management in operating the business.

Reconciliations of these non-GAAP financial measures are included in our earnings announcement, which can be obtained from our website at [www.mastechdigital.com](http://www.mastechdigital.com). As a reminder, we will not be providing guidance during this call nor will we provide guidance in any subsequent one-on-one meetings or calls. I will now turn the call over to Jack for a review of our third quarter 2021 results.

**Jack Cronin**

Thanks, Jenny, and good morning everyone. I'm pleased to tell you that third quarter 2021 was one of our best financial performances since going public in 2008. As Paul Burton is fond of saying, we floated a number of B.O.A.T.s during the quarter. BOATs being the acronym for "Best of All Time".

Our third quarter 2021 revenue totaled a record \$59.5 million dollars compared to \$47.4 million in the third quarter of 2020. This revenue increase represented 26% year-over-year growth and 21% organic growth when adjusting for the AmberLeaf acquisition, which occurred in October 2020. Additionally, this revenue performance was 11% higher sequentially than our results in Q2 2021.

Our Data and Analytics Services segment contributed record revenues of \$10.5 million, compared to \$7.2 million dollars in the third quarter of 2020. After adjusting for AmberLeaf, our organic revenue growth on a year-over-year basis was approximately 19%. Sequentially, revenues were 18% higher than our previous quarter.

During Q3, we continue to see further evidence that the D&A market is in recovery mode. Order bookings were strong for the third consecutive quarter at \$10 million, despite several major orders pushing to Q4; and our pipeline of opportunities continues to show much promise. Still some uncertainty remains in the marketplace with the existence of the Delta variant, but we feel very good about the micro-economic conditions in the D&A space and are very, very optimistic about 2022.

In our IT staffing services segment, we reported record revenues of \$49 million, an increase of 22% on a year-over-year basis and 10% sequentially higher than Q2 2021. Activity levels continued to remain strong in the third quarter of 2021, and we grew our billable consultant base by approximately 5%. Through the first 9 months of 2021, we increased our global consultant base by 24%. That's an annual record and we still have three months to go.

Gross profit in the third quarter of 2021 totaled a record \$16.6 million compared to \$13.1 million in the third quarter of 2020, an increase of 27%. Gross margins as a percent of revenue in the 2021 third quarter was 27.9% compared to 27.6% in the 2020 third quarter.

GAAP net income for Q3 of 2021 was \$3.4 million, or \$0.28 per diluted share compared to \$3 million or \$0.25 per diluted share in Q3 2020.

Our non-GAAP net income for the third quarter of 2021 was \$4.6 million, or \$0.38 per diluted share compared to \$3.8 million or \$0.32 per diluted share in the third quarter of 2020.

SG&A expense items not included in Q3 non-GAAP financial measures, net of cash benefits for the Amortization of Acquired Intangible Assets and Stock-based Compensation and are detailed in our Q3 earnings release, which is available on our website.

Addressing our financial position, at September 30, 2021, we had cash balances on hand of \$5.4 million, outstanding bank debt of approximately \$14 million, no borrowings under our revolving credit facility, and cash availability of \$30 million. Our days sales outstanding measurement increased by three days during the quarter from 63 days at June 30th, 2021. This increase was largely due to two major clients paying us in early October versus on contract terms of September 30th. So while this hurt our days sales outstanding measurement, the impact on our business was really a non-event.

I'll now turn the call over to Vivek for his comments.

**Vivek Gupta**

Good morning, everyone. Thank you, Jack, for the detailed financial review of our operating results for the third quarter of 2021.

It is great to host these calls when you're sitting on record financial results. It's even better when you believe you are well positioned to surpass these if you continue to execute your plan, and that's exactly how I feel today.

Both of our business segments had an outstanding quarter. The Data and Analytics Services segment is experiencing much better market conditions than during the first half of the year, and I'm optimistic that more improvement is in the cards for 2022. Order bookings during the first nine months of 2021 were approximately \$40 million and our pipeline of opportunities continues to improve. Paul will provide more color on the D&A segment in a few minutes.

As for our IT staffing services segment, it continues to "hit the ball out of the park" with 22% year-over-year growth, gross margin expansion, and record non-GAAP operating profits in Q3 of 2021.

Our MAS-REMOTE service offering continues to gain traction and we have successfully expanded this offering to include India based offshore consultants. We believe customers who have become comfortable with the work from home model are ready today to enjoy material cost savings by embracing offshore staffing. We continue to think this concept has both merit and great potential.

With respect to our financial position, we believe we have a solid balance sheet with the linchpin being high quality accounts receivables, which means a strong and predictable cash flow conversion metric. In addition to reliable internal cash generation, we currently have access to capital, sufficient not only to support our existing businesses, but also to capitalize on acquisition opportunities that we believe can better position us in our respective markets. As we have said many times and also demonstrated in the past, inorganic growth is a key element of our overall growth strategy for the future.

I'll now turn the call over to Paul for his comments on our Data and Analytics services segment.

**Paul Burton**

Thank you, Vivek. Good morning, everyone. Q3 represented a discontinuous jump in performance for Data and Analytics. \$10.5 million in revenue was \$1.5 million higher than the previous quarter and, in my opinion, represents a bending of the growth curve.

As I said in my previous earnings calls this year, bookings are a foreboding of revenue to come. The strong bookings in the first half set up our Q3 very nicely, and that can be seen with the results we report today. Although Q3 bookings were below this year's Q1 and Q2, they were still strong; and when you consider that two large deals slipped into Q4 because of their complexity, we remain bullish on revenue over the short to medium term.

Generally, we are finding good acceptance of our Data and Analytics offerings in the market, especially when they are positioned in the context of our emerging cloud capabilities. This has allowed us to continue to sign a high value of long term contracts with our clients, as well as augment existing long term contracts.

We believe that our capabilities in advisory, cloud native application development, and managed services along with Data and Analytics all in the cloud, these things present a strong market opportunity for us and our focus on capture it to not be stronger. We are striking at the heart of our client's digital transformation dilemma and, in so doing, helping them deliver real impact to their business.

Overall, I'm quite happy as D&A continues to become a proportionately larger percentage of overall Mastech revenue and especially operating profit. We expect this not only to continue, but to accelerate as our investments in SG&A and new offerings continue to bear fruit.

Operator, this concludes our prepared remarks. We can now take questions.

**Operator**

At this time, we will be conducting a question and answer session. If you'd like to ask a question, please press "\*" "1" on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press "\*" "2" if you would like to remove your question

from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the "\*" keys. One moment please while we poll for questions. Our first question is from Josh Vogel with Sidoti & Company. Please proceed with your question.

**Josh Vogel**

Thank you, good morning, guys. Thanks for taking my questions. Certainly strong quarterly results. Good work there. I have a couple of questions for you here. I guess I wanted to start with Paul. We're seeing consistent improvement in margins at D&A. Is this sustainable, even as you ramp new engagements, and I know that you were in the mid-fifties last year. How should we be thinking about the margin profile of D&A going forward, even in an environment where you're winning new business at a healthy clip?

**Paul Burton**

Yes, I don't expect erosion in margin going forward. I expect gross margins to be about where they're at, some slight improvement. The reason I say that is if we goose up gross margins, you know, 55, 60% in that area, which is possible by the way, then it prevents us from investing the cash back in the business that we need for growth. So I'd be quite happy with gross margins in the 50 to 52% range and pushing the excess back into the business for growth.

So, I would expect gross margins to say pretty much where they're at, maybe improve a little bit, but our objective is not to jump margins out of the park. Our objective is to apply the cash back into the business for growth.

**Josh Vogel**

Yes, understood. And, when we think about the recent wins earlier this year in Q3, I guess, first, those two projects are engaged slipped into Q4. Was that just the uncertainty around the Delta variant that resulted in that? And then, also when we talk about the build in the business and the business one year to date, is it fair to assume we see a nice sequential step up in D&A revenue in the Q4 similar to what we saw in Q3?

**Paul Burton**

With respect to the two projects that are slipping in or did slip into Q4, didn't have anything to do with the Delta variant. It was purely a matter that they were (INAUDIBLE), additional approvals with for clients which is a good thing to have as the high quality (INAUDIBLE) that you might guess in terms of Q4 revenue, I certainly can't predict or put out a guidance on Q4 revenue but I don't see a problem with Q4 right now.

**Josh Vogel**

Okay, a question for Jack. How should we think about SG&A going forward? You've noted that, you're wired for scale now. We saw that last quarter, but what level of spend do you need to have on a quarterly basis to sustain the growth you see ahead? And understanding that you may need to add headcount in certain from time to time, where do you think those investments would be focused?

**Jack Cronin**

Josh, I think in the short-term, the spend that we have in SG&A in Q3 is about the spend that we're going to have in Q4. We may be up a couple hundred thousand or down a couple hundred thousand, but it's not going to be a material difference.

I really don't even want to comment on 2022. We go through a detailed budgeting process. We look at where we want to spend additional SG&A dollars, if any. So, that's sort of where I think we're going to hit in Q4, more to come on 2022.

**Josh Vogel**

Okay. Can you just talk a little bit about your total liquidity? You mentioned \$30 million in available cash. How much of that is dry powder to explore M&A activity? And then, also just some comments around the costs of your debt, what average interest rate you have today. Thanks.

**Jack Cronin**

Sure. We have \$30 million under our revolving credit facility that's unused. I mean, all of that is in play for acquisitions. We have a good relationship with our lead bank, PNC. Should we do an acquisition, I would suspect that we'd go to PNC and try to get an increase in not only the revolver but an increase in the term loan.

As far as our interest expense, our term loan is priced a little bit higher than our revolver. Our revolver is collateralized with receivable so the risk profile is a little bit lower. But right now, our term loan is priced at 3.5% interest rate. Our revolver is a little bit lower than that, 3%. So today, since we're not borrowing under the revolver, our average cost of debt, pre-tax is by 3.5%.

**Josh Vogel**

That's helpful. Thank you. And if I could sneak in one more or Vivek. Are we getting to a point in the staffing cycle where we might start to see the recovery revert back to more historically seen patterns? For example, we tend to speak Q4 step down a little in Q3, or is there still enough pent out bend out there and structural shifts in the marketplace and people, as you mentioned, being more comfortable in remote work and certainly offshore, do we expect to see this build in Q4 at least for this year?

**Vivek Gupta**

Josh, the demand of course, continues to be really good at this moment. But, we are all getting signals from our customers that the seasonal reduction, which happens towards the end of December on account of Christmas holidays, some forced furloughs and numerous engagements, which just logically come to an end on the 31st of December because the purchase orders run out or whatever the planning process is.

So that seasonality will still show up in Q4, but, on the other hand, the demand still continues to be pretty good and as I've said before in my last call as well, the market is hard. So even the, ends are on a rise. So in Q3, for instance, we had record ends, and of course, we also had record starts. That's how we were able to show the 5% growth. But that kind of situation continues to be there.

**Josh Vogel**

That's helpful. Thank you for taking my questions.

**Vivek Gupta**

Thank you, Josh.

**Operator**

And our next question is from Lisa Thompson with Zacks Investment Research. Please proceed with your question.

**Lisa Thompson**

Good morning.

**Lisa Thompson**

I've been excited to hear you — what's going on over there because of this entire new dystopian world we live in where everybody's quitting or getting fired. And I thought the stock staffing business must be having unusual times. Are things accelerating as far as demand or are people shifting to more remote? And do you think this is going to keep going on? Because I mean, I just keep reading more and more crazy stories about people getting fired from their jobs and then hired back at staffing agencies into the same place. Can you talk about that, and — and do you see this continuing for some while?

**Vivek Gupta**

Sure, Lisa. The market, as I mentioned earlier, is hard. The demand seems to be pretty good and, we are capitalizing on that. We are prioritizing the ones, the opportunities that we can convert, the opportunities that can give us better margins, the opportunities that can give us better volume. So that continues to be there.

We haven't seen evidence of what you just mentioned, which is people getting fired and then they are being hired back through contracts. That we haven't really seen but we haven't seen any change from what we were seeing in the last quarter. The demand continues to be high.

Yes, the consultants have the better opportunities today, in terms of maybe getting better pay or being closer to their family or doing more exciting projects, et cetera. And that is the thing that entices them to leave and move on. But then, at the same time, we are able to attract them as well of it — on almost the same kind of attribute. So it seems to be, you going well. We don't see any immediate signs of this tapering off.

**Lisa Thompson**

And do you feel that you can hire as many consultants in Q4 as you did this quarter?

**Vivek Gupta**

The seasonally, the demand in Q4 is a little less than Q3. Q2 and Q3 are usually the best quarters. So we are going to see a bit of that and the demand will come down, but I'm not saying it's a huge kind of falling off the cliff. It's just a, you know, taper down a little bit and then the end start picking up. And as we say that net growth is an equation, you know, starts minus ends is equal to net growth.

So with ends picking up, I don't know whether we'll be able to get that kind of net growth as we've had, you know, before. We could even have a, you know, remain flat or maybe it could even be a tiny dip, but that's seasonally what is expected and we expect this Q4 to be no different.

**Lisa Thompson**

Okay. And can you talk a little bit more about remote workers based in India? How is that different than plain old MAS-REMOTE? Is it just that they're living in India? How does that work?

**Vivek Gupta**

Well, MAS-REMOTE, basically is a concept that people can be anywhere in the world. I mean, you know, initially, MAS-REMOTE was launched as a concept where consultants could be anywhere else in the United States, but you can easily extend that global level and that's what has happened.

So our customers often times have requirements of skills, which are pretty complex. We call them purple squirrels. They are very hard to find over here in the U.S. at times. And, we are able to find them out of this large pool of IT resources that India has. So by opening MAS-REMOTE up to the Indian consultants, we've been able to bring those high quality, purple squirrels to the customers.

And, the cost arbitrage also works to the customers advantage. They are able to get someone a little cheaper and they're able to save some money and get the right kind of skills. And we are finding that this concept, they were a lot of customers were not amenable to this you know, a couple of quarters ago, but with the world becoming comfortable with working from anywhere, that is beginning to become attractive and we are having numerous conversations with customers on those lines.

**Lisa Thompson**

That sounds great. And I love that term, the purple squirrels. All right. I think everything sounds just one last question about the two deals that you said slipped into Q4, Paul, did those close?



**Paul Burton**

Not yet. Again, the reason they flipped in the Q4 was they required additional approval because of their size, and we're expecting them to close in Q4.

**Lisa Thompson**

Okay, great. Thank you. That's all my questions.

**Operator**

And our next question is from Tim Call with The Capital Management Corporation. Please proceed with your question.

**Tim Call**

Thank you. Just to follow on one of the biggest fears in the last six months was disruption because of the pandemic affecting foreign workers, even though they were working from their homes. I guess, with the pandemic subsiding a little bit in places like India, do you think that's no longer a concern and do you find because they're many of them working from their homes it — in hindsight wasn't a huge uncertainty or do you think because of the pandemic is subsiding in those geographic regions, it's not as big of an uncertainty today?

**Vivek Gupta**

Thank you for your question, Tim. We actually, we were prepared for the worst. We were, sort of expecting maybe the third wave to come to India as well. And, after the second wave, we actually once again went back into shutting down our offices and asking everyone to work from home. And even today, although the virus issue seems to be on the wane at the moment, our teams in both our locations where we have these centers in India, Chennai and in Noida, near Delhi, everyone is still working from home.

And, we are encouraged by the outlook on the Corona front, and we are seeing signs of companies coming back and having their employees come back to the offices. So, we are going to be looking at that. In any case, we don't expect even in the long term and we have made that announcement to our employees last year itself, we don't expect everybody to be coming back full time to the offices.

We are probably going to be 20% of the people working in the offices 20% of the time, and that will be sort of the future way of working. I think, it's not completely over at the moment, but the signs are very positive at the moment.

**Tim Call**

With some businesses requiring vaccinated workers, is a get around of that to have remote workers or contract workers, who are not salaried on board but hired through an agency to fill those jobs that are left open with people who may or may not be vaccinated?

**Vivek Gupta**

Tim, when we look at our entire customer base, I mean customers have different positions on this situation and they could well be, one of the reasons why they are more happy with the remote working because they're able to address this issue or maybe avoid this issue in the process but you know clearly it's every customer has a different position on this.

**Tim Call**

Another fear over the last six months was that as you staffed up for business returning that expenses were going to be front loaded and hopefully revenues would eventually follow with margin recovery - do we see most of that fear behind us as you've staffed up and revenue has started growing? And, we should not fear a large margin degradation because of that staffing up that occurred earlier this year?

**Vivek Gupta**

I'm going to ask Jack to comment on this. Jack, will you take this question?

**Jack Cronin**

Sure. Tim, I think the ramp up in D&A is pretty much behind us. Like I said, Q4, we may be a minor amount higher but the bring back of the austerity measures that we did in 2021 are pretty much baked into our Q3 results. I don't think you're going to see an additional big spike in SG&A going forward.

**Tim Call**

Well, congratulations on a strong quarter and strong outlook and all of your hard work paying off — that's terrific. Thank you.

**Jack Cronin**

Thanks, Tim.

**Vivek Gupta**

Thanks.

**Operator**

And your next question is from Josh Vogel with Sidoti & Company. Please proceed with your question.

**Josh Vogel**

Yes, thank you. I just had a follow-up. I was looking at your 10-Q filing last quarter and saw revenue from India basically double sequentially and it was more than all of 2020 combined. I was just curious, how much revenue came from India in Q3 and what percent of MAS-REMOTE volume is current, I know it's still early days, but what percent of that volume is currently being done with India based consultants?

**Vivek Gupta**

Josh, I'm going to ask a Jack to respond to the first one. But the second one about how much of the MAS-REMOTE volume is coming from India that's actually negligible at the moment in the larger scheme of things because it's only just picking up. We've had probably 1% of our work forces right now working out of India. It's not very significant but the larger question about what is the India revenue, Jack, can you address that?

**Jack Cronin**

We do have work done in our delivery center on the Data and Analytics side. And you're right, our revenues are much higher in 2021 than 2020. In third quarter, I would say we're going to be probably a little under a million in third quarter from work out of India. And, if you look at 2020, that's a healthy increase.

**Josh Vogel**

Great. And it seems like an exciting opportunity to leverage the talent pool over there. And, I understand that it brings lower pay rates that you can basically market to clients with lower bill rates, but is there an opportunity for you to capture greater spread over time by utilizing overseas to consultants?

**Vivek Gupta**

Yes, Josh, that's an exciting possibility and we are looking at ways of fueling the engine more. I think more is going to come over the next few quarters, but we definitely want to add fuel to this fire which is burning quite nicely now.

**Josh Vogel**

Great. Well, thank you again.

**Operator**

Okay. And again, as a reminder, if anyone has any questions, you may press "\*" "1" on your telephone keypad. Doing so will ensure your spot in the question and answer queue. And it appears that we have reached the end of the question and answer session. And I'll now turn the floor back over to Vivek Gupta for closing remarks.

**Vivek Gupta**

Thank you, Operator. If there are no further questions, I'd like to thank you all for joining our call today. And we look forward to sharing our fourth quarter 2021 results with you in early February. Thank you.

**Operator**

And this concludes today's conference and you may disconnect your lines at this time. Thank you for your participation.